An Economic Perspective of Tourism Issues and Policies in Hawaii*

by

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^{*}This paper was originally presented at meetings with the House of Representatives Policy Committee on February 22, 1996 and the Senate Tourism and Recreation Committee on March 5, 1996.

INTRODUCTION

At the dawn of the third millennium, an era that may well become the Asian century, Hawaii is positioned in the middle of one of the most dynamic and fastest growing economic regions in the world. We must have a vision and policies to ensure that our premier economic driver, travel and tourism, remains a viable tool for economic and social development.

In the past, export industries, including travel and tourism, have played important roles in our economy. Over the years, however, the relative importance of the major export industries have changed. U.S. defense and agriculture, the two main industries at the time of Hawaii's Statehood, have since made up a declining share of economic activities in the State. In contrast, tourism, which was an adolescent industry at that time, has mushroomed to become Hawaii's engine of economic growth. Export industries, especially travel and tourism, will continue to play a very important role in our future economic development as they funnel resources into Hawaii which in turn impacts the whole economy, especially those sectors with strong linkages. It is, therefore, imperative that we promote and facilitate development and continued expansion of this sector.

When Statehood came to Hawaii in 1959, it was a time when there were only a few major hotels in Waikiki. However, there has been a significant amount of structural transformation of our economy and the issues are much different today than they were then. At Statehood, we were talking about what economic engines could replace pineapple and sugar. Today we talk about other engines that can take their place along side tourism.

Perhaps more appropriately, we should talk about what will be the driving factors for travel and tourism, how we can diversify tourism, and how we can prepare for the challenges that we are now facing and will likely face in the future. The State's role in travel and tourism is "to maximize the net economic and socio-cultural benefits from tourism to Hawaii's residents." In this regard, we need to identify how the government should rightfully influence tourism in positive directions, and then develop policies and coordinate and implement programs accordingly. As such, we will continue to broaden our focus and increase our role in analyzing tourism trends as well as tourism impacts in order to determine optimum future scenarios for tourism.

This paper presents a public policy vision of the agenda that should be considered for the future. The major salient issues that are addressed include the transformation of the Hawaii economy from agriculture to travel and tourism; the relative importance of tourism today and the differences that exist on the various islands; the need for a greater balance in eastbound and westbound visitor arrivals; the need for additional types of accommodations and airlift capacity; and, finally, how these development efforts can be financed.

THE EMERGENCE OF THE TOURISM INDUSTRY

More than thirty-five years ago, when Hawaii had just become a state, tourism was an adolescent industry. Economic activity was mostly in the U.S. defense and agricultural sectors; together these sectors comprised about 70% of Hawaii's total exports at that time. In contrast, the visitor industry's export share was a modest 14%.

Since then, the Hawaii economy has undergone a dramatic structural transformation. The significance of agriculture, most notably sugar and pineapple, and U.S. defense sector in the State economy has declined; at the same time, the tourism sector has expanded at a phenomenal rate, growing by more than 25 percent annually in certain years. From about 16 percent of

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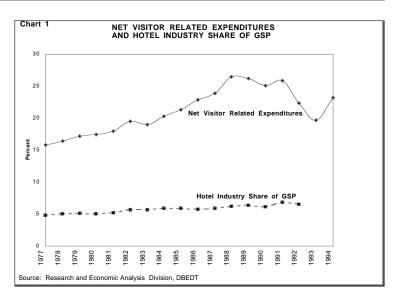
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Hawaii's Gross State Product (GSP) in 1977, the visitor industry grew steadily throughout the 1980s and early 1990s to peak at about 27 percent in 1988. Since that time, tourism has contracted slightly, but remains significant today, accounting for about 20 to 23 percent of GSP (Chart 1).¹

The dramatic growth of Hawaii's tourism industry and the decline of agriculture in the State economy is clear in Chart 2 which compares the percentage share of hotel jobs to agriculture jobs.² Statewide, hotel services accounted for only 1.9% of the total number of jobs in 1960 (Table 1). In that same year, agriculture accounted for 8.4% of the total number of jobs (if food processing, e.g., pineapple and



sugar processing, is included, the share increases to 15.8%).

By 1995, the share of hotel jobs had grown to 6.6%, while the share of agriculture had dropped to 1.9% (or 3.0% if food processing is included). Clearly, the State of Hawaii had undergone a transformation from an agriculture-based economy to a more service-based, tourism-led economy. Closer inspection of the contribution of hotel services and agriculture indicates that the transition point, where hotel jobs equaled and then surpassed jobs in agriculture occurred immediately after 1970, when hotel services accounted for 4.0% and agriculture for 5.1%.

The transition to a tourism-led economy was not consistent statewide in terms of pace and timing, but occurred at different times and to different degrees on each island. For example, as shown in Table 1 and on Chart 2, the transition for Oahu occurred in the mid-1960s; in 1966, the number of hotel jobs equaled that of jobs in agriculture (when one includes food processing, the transition occurs in the early 1970s). Maui appears to be the next island that made the transition from agriculture to tourism, with the switchover taking place in 1978. And by 1980, the number of hotel jobs (14.2%) had surpassed the number of agriculture jobs (11.2%). For Kauai, the transition occurred in 1980. In that year, the number of hotel jobs and agriculture jobs were fairly equal at 10.1% and 9.8%, respectively (the number of total agriculture jobs including food processing was significantly higher at 16.1%). Finally, the Big Island currently appears to be in the midst of the transition from an agriculture-based to a service-based, tourism-led economy. The share of hotel jobs equaled that of agriculture only in 1989 and the shares have since been very close to one another.

Table 1 - Agriculture and Hotel Jobs as a Percent of Total Jobs by State and Counties (1960-1995)

	1960	1975	1985	1995
STATE OF HAWAII Hotel Agriculture	1.9	5.2	6.1	6.6
	8.4 (15.8*)	4.2 (7.1*)	2.9 (5.1*)	1.9 (3.0*)
HONOLULU COUNTY Hotel Agriculture	1.8	4.3	4.4	4.2
	2.9 (7.9*)	1.4 (3.4*)	0.9 (2.3*)	0.6 (1.5*)
HAWAII COUNTY Hotel Agriculture	2.2 27.0 (39.2*)	9.4 17.6 (24.4*)	9.3 13.3 (18.6*)	9.9 8.6 (10.7*)
KAUAI COUNTY Hotel Agriculture	3.0 28.5 (51.0*)	8.9 13.7 (22.0*)	12.3 7.5 (13.1*)	11.9 4.7 (5.8*)
MAUI COUNTY Hotel Agriculture	1.7	9.7	15.9	17.8
	31.3 (49.2*)	15.6 (22.3*)	8.3 (12.0*)	3.8 (5.8*)

*Numbers in parathenses are agriculture and food processing combined. Source: Research and Economic Analysis Division, DBEDT

Even with the slight drop in tourism in recent years,3 the State of Hawaii remains seriously dependent on tourism for its livelihood. In fact, the recent leveling off in Hawaii's tourism is to some extent a sign of maturity of the State's visitor industry. Finding new market segments will be an effective counter to this maturity and will assist in diversification. Thus, promotional efforts must be made to solicit patronage from those seeking medical or extended health care, as well as those interested in Hawaii as a business or sports center. Additional Asian markets should be tapped, and European markets deserve renewed attention. This strategy of market segmentation and product development can help to broaden and expand Hawaii's visitor industry.

Tourism is now clearly the number one industry in Hawaii's economy, affecting nearly every business and individual in the State. As

Hotel HAWAII COUNTY **MAUI COUNTY** Distribution of Agriculture, Food Processing and Hotel Jobs Hotel Agriculture Food Processing Food Processing Agriculture Chart 2 Percent 20 Percent 20 Hotel Hotel Hotel C & C OF HONOLULU KAUAI COUNTY STATE Agriculture Agriculture Food Processing Food Processing Food Processing Agriculture Percent 7 Ŝ Percent Percent

Hawaii's prime exporting vehicle, tourism has fueled the service and retailing sectors, which in turn stimulated other sectors in the economy. In addition to income, the tax revenues generated directly and indirectly from tourism have allowed the State and Counties to fund needed infrastructure, education, and social services to Hawaii's residents.

THE COMPONENTS OF HAWAII TOURISM

Because tourism is one of the main engines of Hawaii's economy, it is important that we continue to diversify within tourism to ensure some stability in the industry and the overall State economy. In focusing our efforts on this task, it is important to understand that tourism is clearly more than just hotel services but includes other services and goods that are directly linked with visitors to the islands. For example, even before arriving at their hotels, tourists must either fly on a plane or sail on a ocean liner to get here. As such, the contribution of transportation (especially air travel) to the visitor industry is significant at more than 10 percent (see Table 2). Upon arrival, tourists enjoy themselves at the beach and engage in shopping, dining, and purchasing of gifts and personal items. Thus, other components of Hawaii's

Distribution

		Distribution
		of visitor
	Visitor share	expenditure
Industry	of total sales	by industry
Agriculture	1.7	0.2
Manufacturing	7.6	1.4
Air Transportation	73.1	6.4
Other Transportation	28.0	3.9
Comm. & utilities	1.4	0.2
Wholesale trade	9.7	1.4
Eating & drinking places	51.0	9.6
Other retail trade	29.4	9.3
Finance, insurance & real estate	0.1	0.0
Hotel services	92.9	28.0
Other services	11.8	6.5
Government	0.1	0.1
Imports	25.1	33.0
Total		100.0

Distribution of direct visitor-related expenditures by industry.

Source: DBEDT, Hawaii 1987 Input-Output Model

Table 2 - Components of Hawaii's Tourism

tourism sector are eating and drinking establishments (9.6 percent), retail trade (9.3 percent), and imports (32.9 percent). At the same time that these industries contribute to tourism, they also rely on the tourist market to a significant degree for their total sales. Visitors' share of hotel services is 92 percent; of air transport, 73 percent; of eating and drinking places, 51 percent; and of retail trade, 29 percent.

Thus, our understanding of the visitor industry needs to be broadened beyond just hotels. In fact, perhaps we should consider referring to "travel and tourism" rather than just "tourism" to remind us of the

need to understand the full implications of our actions vis-à-vis the visitor industry. In recognizing the broader scope of the tourism sector, DBEDT is paying much more attention to the dynamics of the airline industry and its effects on Hawaii. In addition, we are beginning to look more closely at the car rental industry and how government decisions affect the viability of this and other industries.

DIFFERENCES IN THE IMPORTANCE OF TOURISM ACROSS COUNTIES

While the transition to a tourism-led economy occurred at different times on each island, it is also true that the degree of dependence of each island on the tourism sector and the size of the tourism sector on each island today are very different. As shown in Chart 2, the Neighbor Islands are much more dependent on tourism for employment and income than is Oahu. Hotel jobs on Oahu comprise a fairly small share of total jobs (4.2%). In contrast, the share of hotel jobs has grown to more than 17% on Maui. The share of hotel jobs on Kauai, while currently less

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than that on Maui, would most likely be very similar to Maui had it not been for Hurricane Iniki. The importance of the tourism sector on the Big Island is also significantly larger than that of Oahu, though it is slightly lower than Maui and Kauai because of the relatively large agriculture sector in Hawaii County. Therefore, any decision which affects the long-term health or expansion of tourism is even more important for the Neighbor Islands' growth.

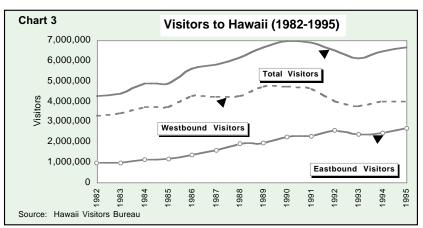
Because the maturity of the tourism sector differs across counties, the approach for future development and growth varies. Tourism surpassed agriculture on Oahu in the mid-1960s and has leveled off since 1980 at about 4 to 5%. On Maui, the switchover took place in the late 1970s, and the tourism sector has shown signs of leveling off since 1990. In both of these islands, it thus appears that additional growth should rely on increasing the **yield** from the visitor industry rather than on simply increasing the number of visitors. In other words, greater emphasis should be placed on raising tourist expenditures per visitor. This can be accomplished through diversification within tourism. Promotion of the convention center, which has the ability to attract higher-spending business travelers, is a good example of how this objective can be accomplished.

For Kauai and the Big Island, there appears to be room for additional growth and marketing can still be directed toward expanding the market. It must be noted that the Big Island, due to its immense size, will perhaps always have a significant agriculture sector alongside tourism.

PROMOTION OF GREATER BALANCE BETWEEN WESTBOUND AND EASTBOUND VISITORS

The expansion of the tourism sector is also evidenced by the number of visitors to Hawaii, particularly since 1982. Although visitor arrivals have been rising in the last two years, we are still below the peak of 1990. As shown on Chart 3, much of this decline is due to a contraction in the westbound (primarily U.S.) market. This market, which accounts for approximately 60% of total arrivals, has declined to mid-1980s levels. On the other hand, eastbound arrivals, primarily the Japanese, have shown steady growth over the past decade except for 1993.

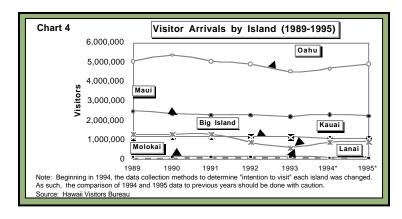
Visitor arrivals increased by 3.2% in 1995 with much of this growth due to a 9.2% increase in east-bound arrivals. Westbound arrivals actually declined by 0.5 percent. This trend is continuing in 1996 with January figures showing a strong 12% growth in eastbound arrivals. In the same month, westbound arrivals increased a modest 2%, but this was fueled by a remarkable 41.3% increase in Canadian traffic. If we look at the U.S. market only, visitor arrivals declined in January (-0.5%) for the fifth straight month.



Despite the modest growth in visitor arrivals across islands varied. As shown in Chart 4, which traces visitor arrivals by island since 1989, arrivals for Oahu exhibit a peak in 1990 while arrivals for other islands are basically flat if not declining slightly. While Kauai has recently experienced growth of more than 5 percent in visitor arrivals, it is clear from the chart that the expansion is largely due to recovery from Hurricane Iniki in September 1992. Clearly, the recent upturn in visitor arrivals is primarily benefiting Oahu.

Much of the reason for the unequal distribution of the benefits of increased arrivals is due to the underlying dynamics of visitor growth. For example, much of the growth statewide was fueled by the eastbound market, but eastbound visitors tend to stay on Oahu and not go to the Neighbor Islands. As shown in Table 3, eastbound visitors account for 40% of total arrivals statewide. However, on Oahu this share is 52%, while for the other islands, eastbound visitors account for 20% or less.

As a result, even though eastbound arrivals grew by 9.2% statewide, the bulk of this growth was experienced only on Oahu (11.4%, see Table 4). Eastbound visitor arrivals for the Neighbor Islands actu-



Westbound Arrivals by Island (1995)					
Island	Total	Eastbound	% of	Westbound	% of
	Arrivals	Arrivals	Total	Arrivals	Total
All	6,633,840	2,656,020	40	3,977,820	60
Oahu	4,915,840	2,562,090	52	2,353,750	48
N. Isles	4,308,600	772,820	18	3,535,740	82
Maui	2,313,170	436,110	19	1,877,060	81
Hawaii	1,075,870	215,330	20	860,540	80
Kauai	919,560	121,380	13	798,140	87

Island	Total	Eastbound	Westbound
AII	3.2	9.2	-0.5
Oahu	4.7	11.4	-1.6
Maui	-1.8	-4	-1.2
Hawaii	-0.3	0.9	-1.2
Kauai	5.2	-15.7	9.4

ally decreased on Maui and Kauai, while they were essentially flat (+0.9%) for the Big Island.

Visitor arrival figures for January 1996 show a similar pattern of strong eastbound growth for Oahu and declines on Kauai and the Big

Island. However, it is important to note that Maui is the exception, showing very strong growth (11.0%). The Big Island experienced a significant reduction in the number of eastbound visitors (-27%) which is most likely due to the federal budget crisis and the resultant temporary closing of the Hawaii Volcanoes National Park.

The tendency of eastbound visitors (primarily Asian) to concentrate their stay on Oahu and not visit the Neighbor Islands is potentially one of the most severe problems

facing Hawaii tourism. This is especially true considering the relatively flat trend in the number of westbound arrivals and the opening of the convention center which is slated for 1998. If this issue is not addressed by marketing programs, this will lead to an increased shortage of visitor accommodation units on Oahu. Without further expansion of westbound visitors to the Neighbor Islands, there will result the unbalanced situation of a shortage of certain types of visitor accommodation units on Oahu and an excess supply on the Neighbor Islands.

To address the imbalance, marketing programs need to be developed which will channel Asian visitors to the Neighbor Islands as well as increase the number of westbound visitors to the State as a higher percentage of this group take Neighbor Island vacations. The use of cultural tourism programs and the creation of special events, such as the Merry Monarch Festival in Hilo, can assist in these efforts. In addition, the Matsuuri and Honolulu Festivals, which are noted for bringing in large numbers of Japanese visitors to Hawaii, provide an excellent opportunity for targeted marketing for Neighbor Island visits. In addition, the Aloha Festivals are Hawaii-specific events that, along with the Japanese festivals, can be promoted in the U.S. to draw additional visitors who may wish to experience cultural events from Asia and the Pacific without leaving the U.S. environment.

THE NEED TO INCREASE CAPACITY

At the same time that the State considers strategies to expand its visitor

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markets and address the imbalance between eastbound and westbound arrivals to the Neighbor Islands, it is equally important that the ability of the State to accommodate the rising numbers of visitors is not overlooked. Over the past thirty years, the number of rooms in the State has grown from 13,000 to over 70,000 today. However, as shown in Chart 5, the bulk of these new rooms has been constructed on the Neighbor Islands resulting in a situation where approximately half of the rooms are on Oahu and half are on the Neighbor Islands. While there are many factors which have led to this situation, one of the most important is the room cap imposed on Waikiki by the City and County of Honolulu. While additional lands have been zoned for resort development outside of Waikiki, most notably Ko'olina and Kuilima, these resorts have not developed as originally envisioned. With the cap on rooms in Waikiki, the number of rooms on Oahu has remained stagnant in the 35,000 range since 1980.

Another important factor which led to this distribution of rooms is the State's land use policies. Many plans over the years, including tourism development plans from the 1960s through the first official statewide tourism plan (1984 State Tourism Functional Plan), espoused policies which provided for a set of self-contained visitor destination areas throughout the state in an effort to spread the "benefits" of tourism development.

However, the "build it and they will come" mentality of these plans combined with a lack of coordinated marketing plans has led to a situation where occupancy rates on the Neighbor Islands are several percentage points lower than those experienced on Oahu. Table 5 lists specific occupancy rates for hotels on Oahu and the Neighbor Islands. Since 1990, occupancy rates on Oahu have been between 76 and 87 percent. This stands in contrast to occupancy rates on Maui, which were generally in the 70 percent range over the period; Kauai, which were in the 60–67 percent range prior to Iniki; and the Big Island, which had the lowest occupancy rates in any given year. In 1995, Oahu's occupancy rate is averaging above 80 percent, while for Maui, it was approximately 75 percent, and Hawaii and Kauai are in the 60-65 percent range. Clearly, Oahu is facing a supply shortage while the Neighbor Islands suffer from low demand.

It is also important to note that the supply shortage for Oahu may have some effect on limiting the number of hotel jobs. A significant increase in the percentage of hotel jobs for Oahu will require changes or shifts in existing policies.

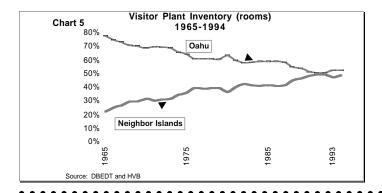


Table 5 - Occupancy Percentage by Island (1990-95)						
Island	1995	1994	1993	1992	1991	1990
Oahu	81.5	80.7	76.4	78.2	79.7	86.6
Hawaii	60.4	63.4	58.2	67	57.4	62
Maui	75.3	72.7	67.5	68.7	73.8	70
Kauai	65.2	75.3	71.4	93.7	59.4	67.4
Statewide	76.6	76.6	71.9	72.8	71.9	79
Source: PKF-Hawaii.						

A recent analysis by DBEDT shows that at its current capacity, Hawaii hotels could accommodate approximately 7.4 million visitors or an additional 720,000 arrivals. Given a 2 to 3 percent growth rate in visitor arrivals, full capacity could be reached in the next 3 to 5 years. This assumes that there would be perfect distribution of the 720,000 visitors on all islands so that overall occupancy is 85 percent (which is thought by many to be full occupancy) for all hotels in the state. If, however, visitors, especially eastbound visitors, continue to concentrate their stay on Oahu and forego visiting the Neighbor Islands, then the existing capacity on Oahu will be reached in even a shorter period of time. As a result, the imbalance in hotel accommodations among the islands will become a problem even sooner.

Data which show that affluent consumers are in a lot better shape today also suggests increased demand for first-class hotel rooms throughout the State. Newly released income data from the Commerce Department for 1994 show that the top 20 percent of households (i.e., those earning in excess of \$60,000) now earn about half of all U.S. income.

The opening of the convention center in 1998 will put additional strain on efforts to balance visitor arrivals throughout the islands. As shown in Table 6, the convention center will likely account for an additional one-quarter of a million visitors in two years time. By 2008, which is only 12 years from now, the convention center will add another 633,600 visitors to Oahu. Certainly, the shortage of first-class rooms on Oahu will become even more severe with the opening of the convention center.

Table 6 - Projected Attendance for Convention Center Events (1998 - 2008)

	1998	2003	2008
No. of Events	36	52	60
Ave. Attendance	5,400	6,200	6,200
Total Attendance	162,000	322,400	372,000
Attend w/ Spouses	255,600	544,300	633,600

Source: Hawaii Convention Center Final EIS, Vol. 1

The degree of the problem in hotel accommodations imbalances across islands depends on the number of upscale rooms available in Waikiki. Upscale rooms will be in high demand by both Japanese and conventioneers. Because there is no generally accepted definition of upscale rooms, the actual count of first-class rooms currently available varies. The HVB hotel room inventory lists the number of upscale rooms at 6,200; the Convention Center EIS estimates the number at 10,000; and Coopers & Lybrand suggests that there are 15,000 upscale rooms in

Waikiki. Despite the different estimates, it is clear that the number of upscale rooms needs to be increased by as much as 50 percent. Note too that the increase in upscale rooms can be accomplished through upgrades and renovations to existing properties, and the actual number of hotel rooms in Waikiki does not need to be increased substantially.

The actual number of visitors displaced to the Neighbor Islands versus those not coming to Hawaii at all due to a low availability of upscale rooms is obviously of great concern, especially considering the high expenditures of Japanese visitors. For example, the Convention Center EIS projects that due to the 633,600 additional conventioneers in 2008, approximately 50,000 Japanese visitors will not come to Hawaii at all. Of the remaining net new visitors to the State (583,600), 77 percent may be accommodated by potential excess room capacity in Waikiki. This means that at a minimum, approximately 130,000 existing visitors to Waikiki will have to be diverted to other resorts on Oahu or the Neighbor Islands.

How many of the 130,000 displaced visitors will be Japanese is difficult to predict although it's generally felt at least one half of the Japanese visitors prefer first- class visitor accommodations and that most Japanese visitors prefer Waikiki as a visitor destination. To ensure that the Japanese visitors can be accommodated in Hawaii, it is imperative that strategies to either channel the Japanese visitors to the Neighbor Islands or make available more upscale rooms in or near Waikiki are formulated as soon as possible. Displacement of the higher spending Japanese visitors with lower spending conventioneers will result in a net loss to the State.

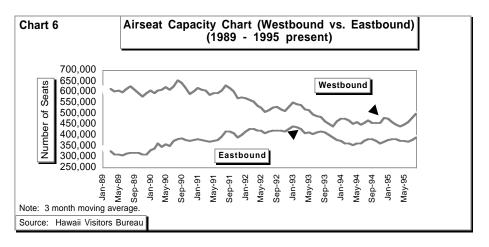
THE NEED TO INCREASE AIRLIFT CAPACITY

During the period from 1989 to 1994, the number of scheduled airline seats to Hawaii have declined faster than passenger counts. In 1989, the number of airseats for both eastbound and westbound flights was 11.0 million; by 1994, this number had fallen to 9.9 million, or a more than 10 percent drop (Chart 6). In contrast, the total number of arrivals over the same period declined by 2.8 percent.

A closer review of the data indicates that the fall in total number of seats to Hawaii is largely due to a decrease of over 30 percent in airlift capacity for westbound flights only. During the same period, airseat capacity on scheduled eastbound flights actually increased by almost 17 percent. As a result, the ratio of eastbound-to-westbound seats changed from 35:65 in 1989 to 45:55 in 1994, indicating the rising importance of foreign, especially Asian, visitors in Hawaii's tourism industry.

While the drop in westbound service has meant fuller flights or higher load factors for the airlines, at

times it was also a limiting factor to the number of visitors to Hawaii. Recent recognition of this has led to air carriers adding additional flights to Hawaii. For example, United Airlines has announced an increase of 7,100 inbound seats per week over the next six months. Of this, one-third (2,600 seats) will be on nonstop flights directly from the U.S. mainland to the Neighbor Islands.



While nonstop westbound flights from U.S. and Canada are increasing, there remain no eastbound nonstop flights from Asia directly to the Neighbor Islands. The inconvenience of having to transfer planes in Honolulu could be one factor which is inhibiting the channeling of eastbound visitors to the other counties. Up until only recently, only Hilo had adequate runways for the landing and take-off of long-distance, wide body aircraft; however, the Keahole-Kona runway is now also of sufficient length to accommodate such flights. In addition, nonstop flights from foreign carriers are controlled by international aviation bilateral agreements between the United States and other countries. Currently, only Honolulu International Airport is designated as a port of entry in many bilateral agreements, including that with Japan.

Because the reasons behind the falling airlift capacity - they include global airline restructuring, lower demand, high percentage of low-paying leisure travelers, rising costs associated with flying to Hawaii, and the government's inability to recognize the key role which the airlines play in the tourism industry - are numerous and the issues are complex, policy options which address the full range of structural issues, in combination with adjustments to cost, are what are needed to ensure greater impact and assist in reversing the downward trend.

Efforts are already underway on the Big Island, with the completion of the Keahole runway, to accommodate direct flights from Japan. DOT is in the process of providing facilities for federal inspection services at Keahole and Japan Airlines has recently filed an application with the U.S. DOT for route authority for daily direct flights to Keahole beginning in April 1996.

In addition, four initiatives can help to lay the foundation to reverse this situation:

- Offer alternatives to the airlines that help to lower the cost of doing business in Hawaii. The airlines expend significant amounts in Hawaii to cover the cost of their operations. Major cost categories that could be reduced include those associated with food and catering, crew travel and incidentals, airport fees, and others.
- 2. Increase marketing and promotion initiatives to increase overall demand, specifically demand by business travelers which generate a better return for the airlines. This is particularly relevant to promotional programs of the convention center.
- 3. Develop Honolulu into a "quasi-hub" with codesharing, particularly with Asian airlines.
- 4. Complete a comprehensive economic analysis on the cabotage issue, with a definitive statement of the costs and benefits for Hawaii.

It is also clear that the airline industry has the perception that they have been taken for granted in Hawaii. As such, the Governor has formed an Advisory Council on Airline Relations, and the Lieutenant Governor will be leading a task force to finds ways to develop a better partnership with the airlines. Of particular importance is the ability to anticipate or appropriately time promotional programs with the periodic discount or "loss-leader" campaigns of the airlines.

In the effort to channel eastbound visitors to the Neighbor Islands, several initiatives need to be continued and perhaps given higher priority. These include the lengthening of runways on all islands to accommodate wide body traffic to assist in opening up these islands to direct flights from Asia as well as the Central and Eastern U.S.

Two projects with high priority are the extension of the airports on Maui (Kahului) and Kauai (Lihue). The \$40 million Maui runway extension and a new \$50 million access road have been on hold due to court action since 1992 over lack of proper environmental documentation. The Department of Transportation completed a State EIS in 1993 and recently completed a federal EIS, and land use changes are in progress through the Land Use Commission.

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Public hearings on Maui for the EIS will need to be completed before the final EIS can be sent to the Federal Aviation Administration. Project design and land use changes could be completed in 1996. If given priority status, this project could be completed by late 1998. Court challenges could, of course, delay this timetable.

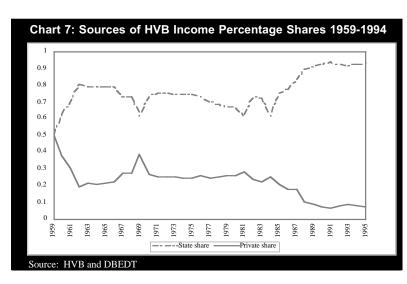
For Kauai, the state and federal EIS need to be completed, and the contracts for project design and construction need to be awarded. This project could be completed before 2000 if given priority status.

THE FINANCING OF TOURISM EFFORTS

At its inception in 1959, the Hawaii Visitor Bureau (HVB) received about one-half of its total budget from the private sector and the other half from the State (Chart 7). Since then, however, the private sector's share has generally followed a declining trend, with dramatic drops since the early 1980s. Currently, DBEDT provides about 90 percent of HVB's budget, or \$23 million annually, for tourism marketing.

This heavy reliance on the State for its budget is partly due to a "free rider" problem in the industry. Over the past several years, HVB's membership has declined substantially. It thus appears that in the absence of sufficiently attractive benefits or penalties to induce contributions by those who benefit from HVB's promotional activities, many businesses choose to "free ride" on the contributions of others. As a result, a sub-optimal level of destination travel promotion is produced and in order to maintain much of the marketing and promotion, government funding is necessary.

To address this problem, a mechanism is needed to assist the visitor industry to engage in collective marketing with a minimal level of government intervention. It is



important to note that several other states countries, including United States, have been moving towards privatization of tourism marketing efforts. shift The funding mechanism other destinations has also been accompanied by a corresponding

change in organizational structure. Importantly, the new funding scheme must be "pro-business."

DBEDT has met with numerous industry leaders to begin evaluating options for financing tourism promotion and to discuss other issues surrounding a fiscal policy for tourism development in Hawaii. In addition, it is now time for HVB to undertake some self-assessment as to its goals, priorities, and activities. For example, in addition to general promotion of Hawaii as a tourist destination, more niche targeting of the market may be fruitful. As was noted earlier, the more affluent consumers have been less affected by the slowdown of the U.S. economy, while other consumers, especially the middle class, have had to cope with lower real income and less leisure (due, for example, to the constraints imposed by two-income families). It would thus appear that targeting of the middle-income group at this time would be less effective in attracting visitors than would a campaign aimed at the more affluent.

"This

heavy

reliance

on the

State

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'free rider'

problem..."

ENDNOTES

¹ Some may recall previous figures which showed a higher value of tourism as a share of GSP. The new lower estimates are the result of revisions made by DBEDT over the past to earlier calculations that underestimated the value of imports in visitor industry transactions, which in turn resulted in an overestimate of the size of the tourism sector. For example, in earlier estimates, the total value of a Gucci handbag sold to a tourist was almost fully counted as a tourist expenditure in GSP; yet Hawaii's value added into the Gucci bag was minimal. In some instances, the underestimate of imports led to as much as a 10 percent distortion in the contribution of tourism to GSP. With the new figures, much of the value of the imported Gucci purse has been subtracted out, leading to a more accurate representation of the relative size and importance of the visitor industry in the economy.

² While tourism is more than just hotel services, jobs in hotel services only is used as a measure of the sector's impact on Hawaii employment since the majority of hotel services is consumed by tourists. As such, the effect of tourism in the analysis that follows understates the true impacts of the visitor industry on the Hawaii economy. Moreover, we are only considering the direct effect on hotels and agriculture; in other words, the linkage effects on jobs and employment are not considered for either sector.

³ The slight decline in tourism's share as a percent of the total economy is not only due to a contraction in the visitor industry but because total GSP and other sectors in the Hawaii economy have been growing at the same time as well. Thus, our economy has become more diversified.